Key points to discuss

- Impact of aid in the Pacific is a source of concern and debate
- Need to rethink ways of delivering aid in the Pacific
- Not necessarily new ideas: rather an acceptance and operationalization of these ideas
- Acceptance by development partners and countries: Has to be done jointly
- Framework applies differently to different PICs
- Stop thinking in terms of aid dependency or exit strategies
- Taking a long term view can improve effectiveness – (did not the Compact try that in N. Pacific?)
Key points to discuss

- Start thinking about how aid can improve delivery of public services in cooperation with the private sector
- A broader definition of international assistance is needed
- Capacity (weak, shallow, thin) – what role for aid?
- Aid can improve governance and improved governance can increase aid effectiveness
- Consider the “Costs” vs Benefits of Sovereignty
- GDP growth may not be the best metric for assessing the impact of aid
Smallness and Remoteness set the PICs apart
Economic Geography: Implications

- Economic geography has implications for economic growth
- Growth is about market access and agglomeration economies
- PICs are not well placed on these counts
- Two takeaways:
  - ‘Right’ or ‘modest’ expectations about growth
  - Focus on delivery of public services (social and infrastructure)
Growth comes in agglomerations

Economic integration between leading and lagging areas increases efficiency but does not guarantee evenly distributed prosperity.
Smallness increases production costs

**Additional Costs of Production Resulting from Smallness**
(Source: Winters and Martin 2004)

The graph shows the additional costs of production in median economies for different sectors:
- **Electronic Assembly**
- **Clothing**
- **Hotels and Tourism**

- **Small economy (4 million)**
- **Threshold (1.6 million)**
- **Very small economy (200,000)**
- **Micro economy (12,000)**

The costs are measured as a percentage of production costs in median economies.
Raising living standards

- What sectors can growth come from?
  - Natural resources, including fish and tourism
  - Niche products

- How can living standards further improve?
  - Labor mobility
  - Remittances

- Improved Infrastructure: Especially connectivity

- Progress on both will require external assistance
  - Technical advice; regulation; infrastructure
Two way (reinforcing) interaction between strengthening public service delivery and increasing incomes

Challenges in improving public services
- Lack of scale economies
- Fiscal revenues will likely fall short of cost
- Capacity constraints
- Governance

Addressing these challenges
- Regional approaches
- Aid (long term)
Regional Approaches
- How to define a region? Sub-regions?

For growth
- Telecoms, transport, energy
- Fisheries, tourism
- Trade and labor mobility

For governance (Pacific Plan)
- transparent, accountable and equitable management of all resources
- a prerequisite for sustainable development and economic growth
Regional provision of services

- National provision is suboptimal
- Economic logic for regional provision is solid
  - Economies of scale
  - Domestic capacity
- So what holds it back?
  - An appropriate grouping of countries
    - Sub-regions due to coordination constraints
    - Contract with nearby large economy
  - Costs
    - Will be higher because currently there is under provision
    - Long-term funding assurance could strengthen regional bodies
  - Notions of sovereignty
Conventional wisdom

Conventional problem:
Aid supports large public sectors $\rightarrow$ squeezes out the private sector $\rightarrow$ [weakens governance] $\rightarrow$ reduces growth

Conventional solution:
Reduce public sectors $\rightarrow$ improve the business environment $\rightarrow$ private sector will grow $\rightarrow$ will generate taxes to pay for public services $\rightarrow$ aid will dwindle $\rightarrow$ economy will be self-reliant
Smaller countries have larger public sectors.
Rethinking conventional approaches

- Reduce public sector ➔ Consider impacts on private sector. And even if ‘large’ how can it improve public service delivery?

- Private sector will grow ➔ And it should, but may not generate sufficient revenues or jobs

- Improve business environment ➔ Yes, but keep in mind what is really needed in a small economy and that regulatory capacity (or market institutions) will be challenged

- Aid will dwindle ➔ Yes, some forms of aid and in some countries. But it could take new forms and modalities. Take a long term view
Aid and Governance

- The technical side of governance or state capacity: Public Financial Management Systems; Economic and Social Statistics; Civil Service

- Does aid harm governance?
- Can aid improve governance?
- Is aid more effective if governance is better?

- Incentives versus capacity
- Supply versus demand for good governance
- Modern versus traditional governance
  - How can they better interact?
We need new ways of delivering aid in the Pacific

Australian State Revenues by Source – 2009
Source: Australian Ministry of Finance

Fiscal transfers between geographical areas are common within and between counties.
Can aid can be viewed as similar to fiscal transfers within countries?

Table 8: Effect of horizontal fiscal equalisation, 2007-08

<table>
<thead>
<tr>
<th></th>
<th>GST pool</th>
<th>Equal per capita distribution of GST pool</th>
<th>Redistribution(a)</th>
<th>Estimated population</th>
<th>Per capita redistribution</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$m</td>
<td>$m</td>
<td>$m</td>
<td>million</td>
<td>$</td>
</tr>
<tr>
<td>NSW</td>
<td>14,858.3</td>
<td>16,883.6</td>
<td>-1,825.3</td>
<td>6.9</td>
<td>-263.4</td>
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<td>VIC</td>
<td>11,275.4</td>
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<td>-1,242.3</td>
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<td>-239.0</td>
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<td>QLD</td>
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<td>10,031.2</td>
<td>58.6</td>
<td>4.2</td>
<td>14.1</td>
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<tr>
<td>WA</td>
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<td>5,091.5</td>
<td>-268.5</td>
<td>2.1</td>
<td>-127.0</td>
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<tr>
<td>WA</td>
<td>4,577.6</td>
<td>3,790.6</td>
<td>787.1</td>
<td>1.6</td>
<td>500.0</td>
</tr>
<tr>
<td>SA</td>
<td>4,577.6</td>
<td>3,790.6</td>
<td>787.1</td>
<td>1.6</td>
<td>500.0</td>
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<tr>
<td>TAS</td>
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<td>1,187.7</td>
<td>646.5</td>
<td>0.5</td>
<td>1,310.6</td>
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<tr>
<td>ACT</td>
<td>933.9</td>
<td>803.2</td>
<td>130.7</td>
<td>0.3</td>
<td>391.7</td>
</tr>
<tr>
<td>NT</td>
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<td>508.8</td>
<td>1,713.3</td>
<td>0.2</td>
<td>8,108.1</td>
</tr>
<tr>
<td>Total</td>
<td>50,614.2</td>
<td>50,614.2</td>
<td>3,336.1</td>
<td>21.0</td>
<td>na</td>
</tr>
</tbody>
</table>

a. The total redistribution of $3,336.1 million is the sum of positive (or negative) items in that column.
A longer-term approach would allow improvements in effectiveness.
A longer-term approach would allow improvements in effectiveness.

<table>
<thead>
<tr>
<th>PEFA Indicator</th>
<th>Fiji</th>
<th>Kiribati</th>
<th>Samoa</th>
<th>Solomons</th>
<th>Vanuatu</th>
<th>Tonga</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual deviation of actual budget support from the forecast provided by the donor agencies</td>
<td>C</td>
<td></td>
<td>C</td>
<td></td>
<td>C</td>
<td></td>
</tr>
<tr>
<td>Completeness and timeliness of budget estimates by donors for project support.</td>
<td>C</td>
<td>D</td>
<td>C</td>
<td>C</td>
<td>D</td>
<td>D</td>
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<tr>
<td>Frequency and coverage of reporting by donors on actual donor flows for project support.</td>
<td>C</td>
<td>D</td>
<td>C</td>
<td>D</td>
<td>C</td>
<td>D</td>
</tr>
<tr>
<td>Proportion of aid that is managed by use of national procedures</td>
<td>C</td>
<td>D</td>
<td>D</td>
<td>D</td>
<td>D</td>
<td>D</td>
</tr>
</tbody>
</table>

Donor practices also need to be improved
Other forms of international assistance are also needed

- Labor mobility can deliver a triple win... with development partners’ support
  - Sending countries
  - Migrants
  - Recipient countries (PICs could be recipients too)

- “Contracting” with large-country regulatory institutions sometimes makes sense
  - Reduced capacity diversion and fiscal costs
  - Assists with economic integration
  - Many existing precedents
Economic growth may not be the best metric for assessing the impact of aid.

By many measures, aid has not failed the Pacific.